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Briefing Report to the Chairman and Ranking Minority Member, Subcommittee on Treasury, Postal Service and General Government, Committee on Appropriations, United States Senate

May 1987

FEDERAL BUILDINGS

Comparison of Oakland and San Francisco Alternatives

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San Francisco Regional Office

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The Honorable Dennis DeConcini
Chairman, Subcommittee on Treasury, Postal Service,
and General Government
Committee on Appropriations

The Honorable Pete V. Domenici
Ranking Minority Member
Subcommittee on Treasury, Postal Service,
and General Government
Committee on Appropriations
United States Senate

In response to your March 19, 1987, request, we reviewed three studies which compare the construction of a new federal building in Oakland, California, to the acquisition of a building now under construction in San Francisco, California. Additionally, we addressed your other questions relating to the impact a move to Oakland would have on employees now working in San Francisco and the additional space requirements that would remain in the Bay area after such construction. On May 4, 1987, we briefed your office on our detailed results. Your representatives requested that we summarize the briefing material and transmit it to you as a formal document.

BACKGROUND

Since 1975, the General Services Administration (GSA) has sought congressional authorization and funding for a new federal building in the San Francisco Bay area to reduce its increasing lease costs. In January 1986, Congress appropriated $8.1 million for the design of a building to be located in Oakland, California, on a parcel of land donated by the city. The city will finance the building under a municipal leaseback arrangement through the sale of taxable municipal bonds. GSA will lease the building for 30 years and acquire the property for a nominal sum at the end of the lease period. The design contract was awarded in January 1987 and about $1.5 million of the design funds had been obligated as of May 1, 1987.

San Francisco officials have objected to GSA's plan to move employees out of San Francisco leased space into the proposed Oakland building. In February 1987, they provided GSA with a study which showed that GSA could save up to $56.3 million over 30 years by purchasing a building in San Francisco. GSA and Oakland subsequently produced studies which showed that GSA could save $51.3 million and $73 million respectively over 30 years by proceeding with the Oakland alternative instead of purchasing the building cited in the San Francisco study.

OBJECTIVES, SCOPE, AND METHODOLOGY

As agreed with your representatives, our overall objective was to determine whether GSA's decision to continue the Oakland project was reasonable in light of the costs and other factors involved. Our specific objectives were to (1) evaluate the cost comparison studies prepared by GSA and by consultants for the cities of San Francisco and Oakland to determine which of the studies most accurately compared the two alternatives, (2) determine how many employees now in leased space in San Francisco would be affected by a move to Oakland and which categories of employee by grade level would be most adversely affected, and (3) determine what additional space requirements would exist in San Francisco if the Oakland building is constructed as planned.

Our review was performed between March 15, 1987, and May 1, 1987, and was conducted in accordance with generally accepted government auditing standards. We (1) analyzed each of the cost studies' criteria and assumptions by interviewing the personnel who prepared the studies and reviewing supporting documentation, (2) used Office of Management and Budget (OMB) approved criteria to perform an independent cost comparison of the two buildings, (3) reviewed GSA zip code data to determine the residences of employees potentially affected by a move to Oakland, (4) determined which employees would be most affected by the move based upon a comparison of the distance between their residences and the two sites, and (5) reviewed GSA's San Francisco space inventory including distribution between owned and leased space.

For our cost comparison analysis, we used criteria contained in OMB Circular A-104 for calculating an economic cost of ownership for capital assets. These criteria, which are used by GSA for such analyses, were used in both the GSA and Oakland cost comparisons. The consultants who prepared the San Francisco study agreed that the criteria were appropriate, but said they did not use them because they lacked sufficient data to apply the criteria in their analysis. In accordance with these criteria, we discounted all figures to present value, assuming a 30-year Treasury bond rate of 7.85 percent. We also assumed a 4.77 percent inflation rate. Both rates were in effect as of April 1987.

EVALUATION OF COST COMPARISONS

We found that none of the three cost comparisons provided a reliable, complete comparison of the two alternatives. Such a comparison should include a life-cycle cost analysis which assesses all costs incidental to the ownership of a facility --acquisition, operation, and maintenance--over its useful life. However, information required to develop all the life-cycle costs such as energy use and component life (roof, air conditioning systems, etc.) were not available for either building and could not be included in our analysis. These costs will be estimated for the Oakland building as part of the design contract. The net cost difference between the buildings could be different if the complete life-cycle costs were available.

Even limiting the analyses to available information, we found that none of the three studies were totally accurate. Our application of the A-104 criteria shows that the planned Oakland building has a 30-year cost advantage of approximately $18.6 million over the San Francisco building. All the cost studies, including ours, made assumptions on occupancy dates, future lease rates, and other factors which are important in determining the final cost advantage. If these assumptions prove to be erroneous, the actual cost advantage could be different. Our assumptions were based on our interpretation of available information and sometimes differed from assumptions made by the other cost studies. Some of this difference can be attributed to the more current and complete information available to us at the time of our review. The more critical differences between the studies--the amount of occupiable square footage in the San Francisco building, the occupancy date for the Oakland building, residual lease costs, and quality differences between the two buildings--are discussed below.

Occupiable square footage

One of the key discrepancies between the cost comparisons concerned the amount of occupiable or usable square footage in the San Francisco building. GSA and San Francisco officials acknowledged that they had used different measurement criteria and that their estimates were highly dependent on final tenant layouts and configurations which are not yet known. For our cost comparison, we applied the standard GSA net to gross floor area ratio (building efficiency) of 80 percent to both the San Francisco and Oakland buildings. Using this ratio, we estimated that the San Francisco building will have approximately 587,000 occupiable square feet, compared to 747,500 square feet for the Oakland building. GSA and San Francisco officials agreed with our methodology for determining occupiable square footage. Both, however, felt confident that this standard will be surpassed in their respective buildings.

San Francisco officials advised us that our comparison of occupiable square footage should include an assessment of how efficient the square footage is likely to be. They argued that their building, because of large floor areas, offers greater efficiency and flexibility in meeting tenant needs than the smaller floors currently planned for the Oakland building. GSA officials pointed out that they are still working with the architects to complete the Oakland building design and that this process is not sufficiently advanced to allow such a comparison. As agreed with your representatives we did not evaluate the efficiency of either building.

Tenant occupancy date

The date the buildings will be available for tenant occupancy is critical in determining the buildings' operating costs and the interim lease costs which would be incurred before full occupancy. For our analysis, we assumed that the Oakland building would be fully occupied in October 1990, the date GSA has projected it will be ready; and that some agencies could move into the San Francisco building during 1988 with full occupancy by January 1989.

San Francisco officials disagreed with our acceptance of GSA's estimated completion date. They maintain that a delay in the projected Oakland building occupancy date is likely; however, the project is currently on schedule, and there is no evidence to suggest that it will be delayed. Any delay for either building would alter the cost comparison. For example, a 1-year construction delay in the Oakland project would lessen the Oakland cost advantage by about $5 million.

Residual lease costs

Another important discrepancy between the cost comparisons concerned the handling of lease costs for those agencies which would move into the Oakland building but could not be accommodated by the smaller San Francisco building. Our analysis assumed that the agencies would remain in leased space at a cumulative 30-year cost of about $63 million. The San Francisco study assumed, however, that GSA would purchase additional space (in addition to the San Francisco building) equal to the size difference between the two buildings. If GSA took such action, the cost advantage for the Oakland building would be greatly reduced. However, GSA officials pointed out that they did not have funding to purchase more space in the San Francisco area. The need for more space would be weighed against other priorities across the country.

Quality costs

Oakland and GSA officials disagreed with our elimination of $18 million in cost they assigned to the San Francisco building to account for "qualitative" differences between it and the Oakland building. They maintain that the Oakland building has clear quality advantages which make it better suited to the needs of federal agencies. They claimed that the San Francisco building lacks certain features that are planned for the Oakland building, such as an auditorium, a raised floor, a granite exterior, freight elevators, and a larger number of toilets. They further claimed that some features of the San Francisco building, such as its wiring systems, are of lower quality than those planned for the Oakland building.

GSA officials said the $18 million represented the cost of these features in the Oakland building; it did not represent the costs which would be incurred to modify the San Francisco building. They pointed out, however, that the estimated cost of the Oakland building included the cost of these features while the estimated cost of the San Francisco building did not.

We did not assign a cost to these differences because it is unlikely that any of these "qualitative" features would be added to the San Francisco building if it were acquired by GSA. The building is nearly complete and some of the features, particularly the raised floor and the auditorium, would be difficult if not impossible to add at this stage.

IMPACT ON FEDERAL EMPLOYEES

Approximately 2,900 employees now in leased space in San Francisco are tentatively scheduled to move to Oakland. The proposed Oakland building, which is 9 miles by car from San Francisco's financial district, is reasonably accessible by public transportation for all employees except those living north of the Golden Gate Bridge, about 5 percent of those affected.

GSA recently conducted a study of the potentially affected employees' residence zip codes. While GSA's data cannot be projected for all employees, they do cover 72 percent of those scheduled to move. Our analysis of these data indicates that 61 percent of the sampled employees could incur additional commute costs and time because they would live further away from the Oakland building than from the San Francisco building, and that 39 percent would either benefit by reduced commute costs and time or would not be affected.

It also appears from our analysis of the study that employees in grades GS-7 and below could be more adversely affected than employees above GS-7. Although these lower-graded employees are about 39 percent of those potentially affected by a move, 44 percent of those who could incur additional commute costs and time as a result of a move to Oakland are in these lower grades.

Officials from both cities said that our analysis of GSA's data did not adequately portray the full impact that a move to Oakland would have on employees now working in San Francisco. Oakland officials said that the overall reductions in commute costs and time for some employees would outweigh the additional costs and time incurred by others. Conversely, San Francisco officials said the difficulties which would be experienced by employees living in areas not directly accessible to Oakland would not only be more costly and time-consuming but also more inconvenient. GSA's data was limited to the residential location of affected employees and did not provide specific information on the actual transportation mode used by these employees. Accordingly, we could not compute actual changes in time or costs as a result of locating in Oakland. We can say only that time and costs would be increased for some employees and decreased for others.

ADDITIONAL SPACE IN SAN FRANCISCO

If the Oakland project is built as planned, GSA would still be leasing about 662,000 square feet in San Francisco based on current estimates. Using GSA's goal of leaving 10 to 20 percent of the inventory in leased space to allow flexibility, GSA could purchase approximately 195,000 to 430,000 additional square feet of space in San Francisco if funding was available. GSA has estimated that the purchase of a 400,000 square foot building would reduce the amount of leased space in San Francisco to 13 percent of the total federally occupied space.

GSA has reviewed nine San Francisco buildings for possible future purchase, two of which have been proposed by city of San Francisco officials as alternatives to the Oakland project including the building considered in the comparative cost analysis. GSA has concluded that four of these buildings are suitable for further consideration but that the other five, including the two proposed by city officials, are not suitable for various reasons. San Francisco officials have proposed a third building--not yet constructed or designed--which has not been evaluated by GSA.

LEASE COSTS RISING NATIONWIDE

GSA is concerned about rising lease costs nationwide. According to GSA officials, the Oakland project represents a potential model solution to the problem of rising lease costs nationally and GSA's ability to effectively manage these costs. GSA anticipates that, as old low-cost leases expire and are renegotiated in cities across the country, lease costs could double--and in some cities quadruple in cost--reaching $2 billion annually by the mid-to-late 1990s.

We have taken the position in past reports that construction and ownership has a lower long-term net budgetary cost in comparison to leasing. Leasing has been favored in practice, however, because of its lower initial budgetary impact. Alternative financing efforts, such as the municipal leaseback arrangement available with the Oakland project, are viewed by many as a way to take advantage of both the cost benefits available through building ownership and the lower annual budget impact available through leasing.

City of San Francisco officials have offered to enter into a municipal leaseback arrangement similar to the one available with the Oakland building. However, GSA officials believe that they have made a commitment to Oakland which has been backed by congressional authorization and which has been made possible by city initiative and cooperation. GSA officials view the Oakland building as a demonstration project for alternate financing and believe withdrawal from the Oakland project at this late date would threaten similar arrangements currently being developed with three other cities and one state.

CONCLUSION

As discussed with your representatives, because of time constraints and the absence of life-cycle data, we could not comprehensively compare the proposed Oakland federal office building with the San Francisco building. The Oakland building design process has not reached a point to allow a complete life-cycle cost analysis or to compare design efficiencies. The cost analysis we did perform favored the Oakland building but is clearly dependent upon assumptions subject to change.

Additionally, other considerations which center on GSA's broader concerns of reducing leasing costs on a nationwide basis must be taken into account in reviewing the proposed alternatives. GSA is correct in seeking ways to reduce these costs and has made a commitment to Oakland which represents a way of reducing lease costs in the San Francisco area. This arrangement represents a potential change in the way the federal government finances its building projects which, by fostering cooperation with local and state governments, could lead to long-term budget reductions.

Based on information currently available to compare the two buildings and taking into account the limitations mentioned above, we believe GSA made a reasonable decision in proceeding with the new federal office building in Oakland.

As requested by your representatives, we did not obtain official agency comments. However, we discussed our methodology and approach with GSA, and city officials from Oakland and San Francisco. These parties generally agreed with our approach but, as discussed previously, had specific disagreements with some of our assumptions. As arranged with your office, we will provide copies of this letter to GSA, the cities of Oakland and San Francisco, and to other interested parties upon request. If you have any further questions, please contact me at (415) 556-6200.

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